

Message Text

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PAGE 01 OTTAWA 01192 01 OF 03 090001Z
ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-08 FRB-01
INR-10 NSAE-00 USIA-15 TRSE-00 XMB-04 OPIC-06
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R 082343Z MAR 78
FM AMEMBASSY OTTAWA
TO SECSTATE WASHDC 6584
INFO AMEMBASSY PARIS
AMCONSUL CALGARY
AMCONSUL HALIFAX
AMCONSUL MONTREAL
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UNCLAS SECTION 01 OF 03 OTTAWA 01192

PARIS FOR USOECD

DEPT. PASS CEA, TREAS, FRB

E.O. 11652:N/A
TAGS: ECON, EFIN, CA
SUBJECT: CANADIAN FOURTH QUARTER AND ANNUAL 1977 GNP.

1. SUMMARY. FOURTH QUARTER GNP SLOWED TO 3.2 PERCENT ANNUAL RATE FROM 5.2 PERCENT RATE IN THIRD QUARTER. REAL CONSUMPTION, INVESTMENT, AND FINAL DOMESTIC DEMAND FELL. SAVINGS RATIO WAS UP. ONLY SOURCES OF FOURTH QUARTER GROWTH WERE GOVERNMENT SPENDING AND FOREIGN DEMAND.

2. FOR ALL OF 1977, REAL GNP ROSE 2.6 PERCENT OVER THE PREVIOUS YEAR, DOWN FROM A 4.9 PERCENT RATE IN 1976.
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PAGE 02 OTTAWA 01192 01 OF 03 090001Z

HOWEVER, FOURTH QUARTER TO FOURTH QUARTER GROWTH WAS 4 PERCENT. GROWTH LED BY EXPORTS WHILE DOMESTIC DEMAND DURING YEAR REMAINED DEPRESSED. REAL CONSUMPTION AND GOVERNMENT SPENDING GREW MODERATELY. PRIVATE INVESTMENT SPENDING DECLINED. IMPORT PRICES ROSE SHARPLY DURING YEAR REFLECTING DEPRECIATION OF CANADIAN DOLLAR AND MADE SUBSTANTIAL CONTRIBUTION TO DOMESTIC INFLATION. NET EXPORTS

OF GOODS AND SERVICES RECORDED DEFICIT OF CDOLS 4.6 BILLION. IMPLICIT GNP DEFLATOR ROSE BY 6.6 PERCENT, DOWN FROM 9.5 PERCENT IN 1976. PATTERN OF GROWTH AND INFLATION REALIZED DURING 1977 SHOWS PROGRESSIVE IMPACT OF CANADIAN DOLLAR DEPRECIATION AND IMPROVEMENT OF REAL FOREIGN BALANCE. GOC SURPRISED AND DISAPPOINTED IN SLOW GROWTH AT END OF YEAR AND FEELS THAT FOURTH QUARTER FIGURES COULD WELL BE REVISED UPWARD. END SUMMARY.

3. REAL GNP ROSE AT ANNUAL RATE OF 3.2 PERCENT IN FOURTH QUARTER OF 1977, DOWN FROM 5.2 PERCENT THIRD QUARTER ADVANCE, PRODUCING AVERAGE ANNUAL GROWTH RATE FOR YEAR OF 2.6 PERCENT. DESPITE SLOWDOWN IN FOURTH QUARTER, GNP GROWTH ACCELERATED IN SECOND HALF OF YEAR. OUTPUT ROSE BY 4 PERCENT BETWEEN FOURTH QUARTERS OF 1976 AND 1977. EXPANSION LED BY STRONG EXPORT GROWTH, WHILE FINAL DOMESTIC DEMAND REMAINED DEPRESSED. DISCUSSION OF DEVELOPMENTS OF MAIN GNP COMPONENTS IN FOURTH QUARTER AND FOR YEAR AS WHOLE FOLLOWS BELOW.

4. CONSUMPTION. NOMINAL DISPOSABLE INCOME ROSE 2.7 PERCENT IN FOURTH QUARTER. PERSONAL CONSUMPTION PRICE INDEX ADVANCED BY 1.8, GIVING 0.9 RISE IN REAL DISPOSABLE INCOME. REAL CONSUMPTION SPENDING DECLINED BY 0.4 PERCENT DUE TO RISE IN SAVINGS RATIO FROM 10.4 PERCENT TO 11.2 PERCENT. WEAKNESS OF CONSUMPTION SPENDING IN GENERAL UNCLASSIFIED

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PAGE 03 OTTAWA 01192 01 OF 03 090001Z

IN FOURTH QUARTER AND RISE IN SAVINGS RATIO IN PARTICULAR SEEMS ANOMALOUS IN LIGHT OF ACCELERATION OF RETAIL SALES DURING PERIOD. FOR 1977 AS A WHOLE, REAL CONSUMPTION WAS UP BY 2.8 PERCENT. ACCELERATION OF INFLATION DURING 1977 COMBINED WITH PROGRESSIVE MODERATION OF NOMINAL WAGE INCREASES, RESTRAINED GROWTH OF REAL INCOMES AS DID SHARP DECLINE IN NET FARM INCOME.

5. INVESTMENT. DEPRESSED INPART BY SUBSTANTIAL EXCESS PRODUCTIVE CAPACITY, PRIVATE FIXED INVESTMENT DROPPED BY 2.7 PERCENT IN FOURTH QUARTER AND BY 1.2 PERCENT ON AVERAGE IN 1977 FROM 1976 LEVEL. RESIDENTIAL CONSTRUCTION AND MACHINERY AND EQUIPMENT INVESTMENT DECLINED. CONSTANT DOLLAR INVENTORY INVESTMENT ROSE BY CDOLS 104 MILLION IN FOURTH QUARTER FOLLOWING CDOLS 168 MILLION RISE IN THIRD AND DECLINED BY CDOLS 64 MILLION FOR YEAR AS WHOLE. AVERAGE ANNUAL RISE IN AFTER TAX CORPORATE PROFITS WAS 18.8 PERCENT. INCREASE IN GOVERNMENT INVESTMENT SPENDING (3.2 PERCENT) AND IN NON-RESIDENTIAL CONSTRUCTION (3.7 PERCENT) PARTIALLY OFFSET STRONG DECLINE IN OTHER INVESTMENT COMPONENTS WITH RESULT THAT REAL GROSS FIXED CAPITAL FORMATION WAS ESSENTIALLY STAGNANT FOR YEAR.

GOVERNMENT SECTOR. TOTAL GOVERNMENT SPENDING ROSE AT ANNUAL RATE OF 7.6 PERCENT IN FOURTH QUARTER WITH BULK OF INCREASE ACCOUNTED FOR BY HIGHER UNEMPLOYMENT INSURANCE PAYMENTS. FOR YEAR 1977, TOTAL GOVERNMENT EXPENDITURES ADVANCED BY 11.2 PERCENT, A REAL INCREASE OF ABOUT

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PAGE 01 OTTAWA 01192 02 OF 03 090011Z
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UNCLAS SECTION 02 OF 03 OTTAWA 01192

3.5 PERCENT (I.E., MORE THAN GNP GROWTH). ,EEL# GOVERNMENT PURCHASES OF GOODS AND SERVICES INCREASED BY 2.3 PERCENT. REVENUES WERE FLAT IN FOURTH QUARTER AND UP BY 8.6 PERCENT ON AVERAGE IN 1977. GOVERNMENT SECTOR DEFICIT (INCLUDING NON-BUDGETARY TRANSACTIONS) IN 1977 WAS CDOLS 5.7 BILLION OR 2.7 PERCENT OF GNP.

6. FINAL DOMESTIC DEMAND. DUE TO WEAKNESS OF CONSUMPTION, INVESTMENT AND GOVERNMENT SPENDING, REAL FINAL DOMESTIC DEMAND DECLINED AT ANNUAL RATE OF 2.4 PERCENT IN FOURTH QUARTER AND EXPANDED BY ONLY 1.9 PERCENT FOR YEAR.

7. PRICES. IN PART DUE TO DEPRECIATION OF CANADIAN DOLLAR, IMPORT PRICES INCREASED BY 11.6 PERCENT ON AVERAGE FOR YEAR AND ADVANCED BY 16.6 PERCENT BETWEEN FOURTH QUAR-

TERS OF 1976 AND 1977. GNP DEFLATOR ROSE 6.6 PERCENT BUT
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PAGE 02 OTTAWA 01192 02 OF 03 090011Z

PERSONAL CONSUMPTION DEFLATOR WAS UP 7.3 PERCENT AND CPI
8.1 PERCENT, REFLECTING THE GREATER WEIGHT OF IMPORTS IN
CONSUMPTION EXPENDITURES THAN IN GNP AS A WHOLE.

8. EXTERNAL SECTOR. STRONG GROWTH OF EXPORTS WAS MAIN
SOURCE OF GROWTH IN 1977. REAL EXPORTS OF GOODS AND
SERVICES INCREASED BY 7.7 PERCENT; REAL MERCHANDISE EXPORTS
EXPANDED BY CLOSE TO 10 PERCENT. IN CONTRAST, REAL IMPORTS
OF GOODS AND SERVICES ROSE BY JUST UNDER 2 PERCENT, AND
MERCHANDISE IMPORTS INCREASED BY 1.1 PERCENT. MOVEMENT OF
IMPORT VOLUMES CLEARLY REFLECTS POSITIVE INFLUENCE OF
CANADIAN DOLLAR DEPRECIATION ON REAL FOREIGN BALANCE. EXPORT
AND IMPORT PRICES INCREASED BY 7.4 PERCENT AND 11.8 PER-
CENT RESPECTIVELY. THUS, VALUE OF GOODS AND SERVICES
EXPORTS INCREASED BY 15.6 PERCENT AND IMPORT VALUE BY 14
PERCENT PRODUCING CDOLS 4.6 BILLION DEFICIT ON BALANCE
OF GOODS AND SERVICES TRANSACTIONS. ASSUMING POSITIVE
BALANCE OF ABOUT CDOLS 500 MILLION ON TRANSFERS, CURRENT
ACCOUNT DEFICIT FOR 1977 WOULD BE CDOLS 4.1 BILLION.

9. COMMENT. TIME PATH OF GROWTH AND INFLATION. COMPARISON
OF AVERAGE GROWTH AND INFLATION RATES IN 1977 WITH CHANGES
IN THESE MAGNITUDES BETWEEN FOURTH QUARTERS OF 1976 AND
1977 SHOWS BOTH GROWTH AND INFLATION ACCELERATING AND REAL
FOREIGN BALANCE IMPROVING OVER THE COURSE OF 1977.

A. REAL GNP ADVANCED BY 2.6 PERCENT ON AVERAGE FROM 1976,
BUT ROSE BY 4 PERCENT ON FOURTH QUARTER OVER FOURTH QUAR-
TER BASIS, SHOWING TENDENCY OF REAL GROWTH TO ACCELERATE
DURING YEAR.

B. MAIN FACTOR GENERATING FASTER GNP GROWTH WAS REAL
EXPORTS WHICH ROSE BY 7.7 PERCENT ON AVERAGE AND BY NEARLY
10 PERCENT FROM FOURTH QUARTER 1976 TO FOURTH QUARTER 1977.
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PAGE 03 OTTAWA 01192 02 OF 03 090011Z

GROWTH RATES FOR REAL IMPORTS WERE 2 PERCENT AND MINUS 2
PERCENT RESPECTIVELY BY THESE SAME TWO MEASURES. THUS,
REAL FOREIGN BALANCE SHOWED CONTINUING TREND TOWARD IMPROVE-
MENT DURING YEAR, REFLECTING PROGRESSIVELY LARGER IMPACT
OF CANADIAN DOLLAR DEPRECIATION.

C. SIMILAR MOVEMENTS EVIDENT IN TIME PATH OF INFLATION.
IMPORT PRICES ROSE BY 11.8 PERCENT ON AVERAGE IN 1977, BUT

BY 16.6 PERCENT DURING THE YEAR. PATTERN OF IMPORT PRICE
RISE MIRRORED IN TREND OF PERSONAL CONSUMPTION DEFLATOR
WHICH SHOWED AVERAGE RISE OF 7.3 PERCENT AND FOURTH QUAR-
TER TO FOURTH QUARTER ADVANCE OF 8.2 PERCENT.

10. DEPARTMENT OF FINANCE'S OFFICIALS TOLD EMBOFF THAT
THEY HAD EXPECTED REAL GNP TO GROW AT 5 PERCENT ANNUAL RATE
IN FOURTH QUARTER AND WERE SURPRISED AND DISAPPOINTED
AT ACTUAL OUTCOME. THEY NOTED THAT THERE WERE MAJOR DIS-
CREPENCIES BETWEEN INCOME AND EXPENDITURE SIDES OF NATIONAL
ACCOUNTS IN FOURTH QUARTER (TOTAL INCOME LESS THAN TOTAL
EXPENDITURE) AND THAT EXPENDITURE AND REAL GNP FIGURES
FOR FOURTH QUARTER COULD WELL BE REVISED UPWARD.

11. TABLE. 1977 REAL GNP AND COMPONENTS, SEASONALLY
ADJUSTED ACTUAL PERCENTAGE CHANGE BETWEEN THIRD AND FOURTH
QUARTER, ANNUAL AVERAGE CHANGE FROM 1976 TO 1977 AND CHANGE
BETWEEN FOURTH QUARTER 1976 AND FOURTH QUARTER 1977.
BRACKETS INDICATE DECREASE.

-----	1977IV	1977 AVERAGE/	1977IV
-----	1977III	1976 AVERAGE	1976IV
PERSONAL CONSUMPTION (0.4)	2.8	0.9	
GOVT. CURRENT SPENDING(0.8)	2.2	2.9	
GOVT. INVESTMENT	1.6	3.2	8.6
PRIVATE INVESTMENT	(2.7)	(1.2)	(2.3)

NOTE BY OC/T: #AS RECEIVED.

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PAGE 04 OTTAWA 01192 02 OF 03 090011Z

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PAGE 01 OTTAWA 01192 03 OF 03 090012Z

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UNCLAS SECTION 03 OF 03 OTTAWA 01192

-----1977IV 1977 AVERAGE/ 1977IV
-----1977III 1976 AVERAGE 1976IV

CHANGE IN INVEN-

TORIES1	104	(64)	NA
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EXPORTS	4.7	7.7	9.9
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OF WHICH:

MERCHANDISE	5.6	10	12.2
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IMPORTS	(1.5)	2	(2.0)
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OF WHICH:

MERCHANDISE	0.5	1'1	(1.8)
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PAGE 02 OTTAWA 01192 03 OF 03 090012Z

GNP	0.8	2.6	4
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FINAL DOMESTIC

DEMAND	(0.6)	1.9	0.9
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MILLIONS OF 1971 CANADIAN DOLLARS. ENDERS

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